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No. 838

Supreme Court of the United States

OCTOBER TERM, 1964

CAROLINA & NORTHWESTERN RAILWAY COMPANY, ATLANTIC & EAST CAROLINA RAILWAY COMPANY, STATE UNIVERSITY RAILROAD COMPANY and SOUTHERN RAILWAY COMPANY, *Appellants*,

v.

THE UNITED STATES OF AMERICA, INTERSTATE COMMERCE COMMISSION and LOUISVILLE AND NASHVILLE RAILROAD COMPANY, *Appellees*.

ON APPEAL FROM THE UNITED STATES DISTRICT COURT FOR THE WESTERN DISTRICT OF NORTH CAROLINA

BRIEF FOR APPELLANTS IN OPPOSITION TO MOTIONS TO AFFIRM

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The appellees' motions are compounded of irrelevancies, disagreements between themselves and reiteration of the theme that the judgment below should be affirmed because the questions presented on this appeal cover matters within the supposed expert discretion of the Interstate Commerce Commission as to which its judgment is conclusive. That is not an accurate view of this case or of the applicable law. The Commission, like any other agency, is bound by the terms of the statute it administers. And, like any other agency that decides cases on a record, it is subject to the requirement of Section 8(b) of the Administrative Procedure Act that its decision include a statement of "findings and conclusions, as well as the reasons or basis therefor, upon all material issues of fact, law, or discretion presented on the record." Those limita-

tions on the Commission's power are judicially enforceable in the interest of guarding against unlawful and arbitrary administrative action. The Commission here did not comply with the governing statute or make appropriate findings on the issues of fact and law encompassed by the questions presented in this case or state comprehensible and rational grounds for its resolution of them.

The importance of this case is not confined to the particular divisions involved. Southern participates in joint movements of coal with other railroads in the geographical area involved in this case; there are other joint movements of coal in that area in which the Southern is not a participant. The Commission's decision disrupts the basis on which all of these coal divisions have been established for many years. The decision will doubtless be regarded by other carriers as establishing a pattern for the re-division of revenues from the carriage of coal throughout the southeastern part of the United States. For that reason the questions presented are likely to arise again both before the Commission and in the courts. The Commission's decision should not be allowed to serve as a precedent if it does not comport with the statute and if it is not supported by adequate findings and reasoning.

I. WHAT IS AT ISSUE

The L. & N. devotes nearly two pages of its motion to answering an argument that appellants do not make in this Court (L. & N. Motion pp. 5-7)—that the Commission erred in its conclusion that as to all other relevant factors things were equal as between the contending carriers and in its consequent decision to rely solely on the relative costs of the carriers. The Commission's exclusive reliance on costs, which is not contested here, make extraneous all of the discussion

in the motions concerning the purported lengthening of the L. & N.'s haul over the years, the purported burden upon it of originating the coal movement and other matters on which the appellees dwell (L. & N. Motion pp. 2-4; Gov't Motion pp. 2-4). The Commission's decision to rest its determination on costs alone made it essential that the Commission measure the actual relative costs of the carriers—not fictitious costs—and that in doing so it should not, without rational explanation or grounds, adopt methods that have no sanction in logic, authority, experience or the Commission's own accounting standards. The Commission's report and the cost findings of its hearing examiner show that it disregarded these limitations on its authority. That is the substance of appellants' complaint.

The appellants do not, as the Government contends, concede "that marked changes in circumstances since 1918 have rendered the old method of division unjust to the L. & N., and that new divisions should be prescribed pursuant to Section 15(6) of the Act" (Gov't Motion pp. 5-6). Both the Commission's determination that existing divisions were unlawful and its prescription of new divisions for the future, both made pursuant to Section 15(6), were based upon costs. If the Commission erred in its computation of costs, then the finding of unlawfulness as well as the prescription of new divisions for the future is affected by the error.[1]

[1] Appellants have stated without contradiction that correction of the three errors of the Commission discussed in the Jurisdictional Statement would reduce from $540,000 to $226,149 the annual shift of revenues from the Southern to the L. & N. (Jur. St. p. 15). Correction of other errors that appellants would deal with on plenary consideration of the case (*id.* p. 22), would result in a showing that the L. & N. receives no less from existing divisions than its costs entitle it to.

II. THE STATUTORY ISSUE

Appellants contend that the Commission decision, in its adoption of a mistaken theory of comparability of costs, reflects a misunderstanding of the congressional direction in Section 15(6) that the Commission consider "the amount of revenue required to pay . . . [the carriers'] respective operating expenses, taxes, and a fair return on their railway property held for and used in the service of transportation . . . ." (Jur. St. pp. 16-18). The L. & N. says that in making this contention appellants themselves misread the governing statute. (L. & N. Motion pp. 8-10).

To be sure, the quoted clause of the statute covers the matter of relative systemwide revenue needs of the carriers dividing joint rates, as the L. & N. says; the Commission found in this case that neither carrier stood in greater need of revenues than the other (Jur. St. p. 30a). But the clause covers more. It covers in addition the matter of the relative costs of the carriers for the particular service in issue. That was made clear by this Court in *Baltimore & O.R.R.* v. *United States,* 298 U.S. 349, 360 (1936). See also *Divisions of Freight Rates,* 165 I.C.C. 94, 100-01 (1929) (Commissioner Eastman). Moreover, it has never been suggested that in either aspect the statutory provision authorizes the Commission to determine anything other than actual "operating expenses" of the carriers.

The Government does not make the same statutory argument as the L. & N. It does not, as the L. & N. appears implicitly to do, claim for the Commission the power under the statute to substitute fictitious or hypothetical costs for the actual relative costs of the carriers, as best they can be determined. It does, however, join with the L. & N. in seeking to sustain a decision in

which the Commission did just that, as we have shown in our Jurisdictional Statement and as we shall again demonstrate below.

III. THE COMMISSION'S FINDINGS AND REASONING

A. Reproduction Value

The Commission was explicit that it used reproduction value in computing the car costs of the L. & N. because "the per diem charges paid by the Southern were determined upon a reproduction cost basis," and the use of reproduction value for the L. & N. "makes comparable these costs as between the complainant and the defendant placing them on an equal footing." (Jur. St. p. 25a).

The demonstrated infirmity, in both law and logic, of this concept of comparability (Jur. St. pp. 19-20) prompts the appellees all but to ignore the only reason stated by the Commission for its use of reproduction value in computing the L. & N.'s car costs. They make no more effort than did the Commission to explain why its conclusion follows from its premise. The appellees turn instead to a rationale for the use of reproduction value here that would justify its use, not just in this divisions case, but in every rate case before the Commission. (L. & N. Motion p. 11; Gov't Motion pp. 6-8). They say, in substance, that because the cost of cars has risen the use of original cost for computing depreciation would not adequately compensate the L. & N. This is a rationale that the Commission did not offer, and it thus runs afoul of the elementary rule that an agency order is judged by the reasons assigned by the agency and not reasoning supplied by the agency's lawyers on appeal or by a private litigant. *Burlington Truck Lines, Inc.* v. *United States,* 371 U.S. 156, 168-69

(1962); *SEC* v. *Chenery Corp.*, 318 U.S. 80, 87-88 (1943). Moreover, the Commission itself would presumably disown the reasoning because for many years it has used original cost in determining the justness and reasonableness of rates.[2] Thus the pleas of the L. & N. that the use of original cost would not reflect the "true economic value" of its cars and of the Government lawyers that "the cost of replacement of the L. & N.'s coal cars at current prices would exceed the present book value of its entire fleet of some 60,000 freight cars" should be addressed to the Commission in its rate-making capacity, not used in support of a decision in which, whatever else may be said of it, the Commission plainly did not conceive of itself as deserting the original cost precepts that it has applied for many years with the sanction of this Court.

B. Time and Mileage Separation

The appellees again disagree with each other when they seek separately to justify the Commission's action in attributing all of the L. & N.'s car repair and depreciation costs to the passage of time and none to the use made of the cars.

The L. & N. thinks that the hearing examiner's statement that to relate car costs to both time and use would cause "severe penalties" to the L. & N. is an adequate "finding" to justify a method of computing costs that disregards the way in which they are actually incurred. (L. & N. Motion pp. 10-11). The Government, on the other hand, apparently thinks that

[2] The statement of the Commission about the replacement cost of the L. & N.'s hopper cars, to which the Government refers in its discussion of this point (Gov't Motion p. 7), was not made in connection with the Commission's treatment of costs but in quite a different context. (Jur. St. p. 14a; see Jur. St. p. 24a).

the failure to make the time-mileage separation was permissible because to make it would have caused scarcely any penalty at all to the L. & N. (Gov't Motion pp. 8-9). At any rate that is what the Government seems to say after first making the curious argument that the Commission could properly disregard the separation because the appellants' cost studies were based both on time and mileage and original cost, and the Commission correctly declined to adopt those studies because of their failure to use reproduction value. There is no relationship between the time and mileage computation and the question of original cost. The argument seems to assume that if an agency is entitled to reject one aspect of a litigant's evidence it is entitled to reject a different and unrelated aspect without any consideration of its merits. This is an extraordinary view of the duty of an administrative agency. It was the obligation of the Commission to appraise each factual issue on its own merits and if necessary to probe for facts that would provide a rational basis for resolution of the issue.

The Government acknowledges, moreover, that no real probing was necessary—that the figures on which to base a time and mileage separation were available to the Commission on the record in the evidence of the L. & N. Its ultimate conclusion is that the Commission was justified in disregarding those figures because they would not have made much difference anyway and so it was "administratively more appropriate"—which must mean "easier"—to attribute all car costs to the passage of time, even though depreciation and repairs are in major part a function of use. That, once more, is not the reason assigned by the Commission for its action; its only reason was that given by the hearing

examiner, which the Government does not even bother to note and in substance disavows.[3] Moreover, the reason now given by the Government on appeal is plainly inadequate. The $20,398 reduction in the L. & N.'s costs, which is what the Government says would result from making the time-mileage separation, means, in this case where a divisional scale was made to relate directly to costs computed for a four-month test period, a shift of $61,000 in annual revenues from the L. & N. to the Southern. This loss to the Southern will recur each year throughout the indefinite period in the future in which the prescribed scale of divisions will be applied. The amount involved cannot be dismissed as insignificant.

C. The Per Diem Credit

Neither appellee is willing to subscribe to the hearing examiner's stated reasons, adopted by the Commission, for failing to give full instead of partial effect to the Southern's per diem payments as an offset to the L. & N.'s car costs. This is altogether understandable because the examiner's treatment of the matter is very murky indeed. It is true, as the Government points out (Gov't Motion p. 10), that he confused two separate matters: (1) the overall position of the L. & N. as a net lessor of freight cars and its consequent systemwide excess of per diem income

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[3] The Government at one point in its motion refers to "lengthy findings" as to relative costs made by the hearing examiner and adopted by the Commission, as if a citation to the number of pages on which the examiner dealt with costs is by itself a refutation of our contention that findings on the points here at issue were inadequate. (Gov't Motion p. 7 n.5). We submit that there is nothing in the pages cited by the Government going to those points beyond what we have quoted or paraphrased in our Jurisdictional Statement.

over per diem outgo, and (2) the excess in this movement of the per diem payments it receives over the car costs it incurs during the period for which it receives per diem payments. Nevertheless, the examiner did find "that there is a spread between actual car costs of the L. & N. and rentals received from the Southern on the Knoxville coal traffic . . . ." (Jur. St. p. 50a). And regardless of that, it cannot be denied that there is such a spread. The L. & N. does not deny it.[4] The Government at two points seemingly affirms the existence of the spread when it states or accepts the statement that the L. & N.'s car costs were $1.78 per car day (Gov't Motion pp. 8, 9), while the per diem rate was $2.75. Yet, in the concluding paragraph of its argument the Government baldly states that there was no showing in the record "that *any* net credit accrues to the L. & N. from its car rentals to the Southern in connection with the coal traffic here in question." (Gov't Motion p. 10). There are some problems in transportation economics that, "unlike a problem in calculus, cannot be proved right or wrong," *New York* v. *United States*, 331 U.S. 284, 328 (1947) (Gov't Motion p. 10), but this is not one of them. A dollar and seventy-eight cents is less than $2.75, and that means that the L. & N. had a net credit from car rentals in

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[4] The L. & N. does take exception to our pointing out that most of the cars used in the movement were old 50-ton hopper cars, which is one of the factors making the rentals it receives larger than the costs it incurs. (L. & N. Motion p. 4 n.4). Simple arithmetic shows that in the four months used as a test period for computing costs, most L. & N. cars were 50-ton cars. In that period 7,906 cars (Jur. St. p. 10a) moved 437,196 tons of coal (*id.* p. 38a). That is an average of 55.3 tons per car. A fully-loaded car of nominal 50-ton capacity carries about 55 tons of coal. The L. & N. has purchased no 50-ton hopper cars since 1951. (Exs. C-26, C-28).

this movement.[5] The Government is plainly wrong and the appellants and the hearing examiner are right.

For the rest of their discussion of this point, the appellees rely on what can be termed the "landlord" argument. (Whatever the merits of this argument, it bears emphasis that it is the appellees' argument on appeal; it is not reflected in the Commission's report or in its hearing examiner's decision.) In effect, the appellees say that the situation here is just as if the L. & N., independently of its railroad operations, were the owner of facilities that the Southern leased from it. In such a case the Southern's rental payments would be a part of its costs to the extent that the facilities were allocable to the movement in issue, but the L. & N.'s receipts would have nothing to do with its divisions. This is a wholly unrealistic view of the problem that the Commission faced in this proceeding. The Government's uniquely narrow reading of the statutory words "transportation service" as being limited to a carrier's operations on its own line (Gov't Motion pp. 9-10) does not make it any less so.

Moreover, it is not the view that the Commission takes when it focuses on the question rather than ignoring it, as it did in this case. In *Akron, C. & Y. R.R.* v. *Atchison, T. & S.F. Ry.*, 321 I.C.C. 17, 43 (1963),[6] the

[5] In the L. & N.'s exhibits three separate figures for its car costs per car day are set forth, and none of them approaches $2.75. The figures are $1.34, based on original cost (Ex. C-200, Sheet 2), and $1.43, based on original cost, and $1.78, based on reproduction value (Ex. C-257, work table 14, footnote 2, sheet 1 of 9).

[6] This is the transcontinental divisions case, in which the Commission's order was set aside, on grounds unrelated to the point under discussion. Atchison, T. & S.F. Ry v. United States, S.D. Cal. No. 63-745-EC, decided Jan. 25, 1965. Notice of appeal to this Court has been filed.

Commission found that the Group I costs (car costs) of a given railroad, as computed according to its costing formula, Rail Form A,

> "include principally car repairs, depreciation, and return on all cars owned. Per diem payments for foreign cars serving on this road are added, and per diem receipts from home cars serving on a foreign road are subtracted. The inclusion of per diem settlements adjusts the costs from the basis of cost of cars owned to the basis of cost of cars serving on the road. These latter costs are divided by the service car-miles to give a cost per car-mile. Thus, if per diem is more or less than car ownership costs, a substantial difference can result: a difference which represents actual dollars paid out or received."

The Commission made clear that it approved of this procedure. *Id.* at 44. If the procedure had been followed in this case, just what we have said should have been done would have been done: the L. & N.'s costs of car repairs, depreciation and return on all cars owned by it and used in the movement would have been computed and from these costs its per diem receipts from cars serving on the Southern would have been subtracted; there would have been no per diem payments to add because the L. & N. supplied all the cars, and for the same reason the Southern's per diem payments properly were computed as its only car costs. The error of the Commission lay in its unexplained failure to subtract from the L. & N.'s total car costs the entire amount of its per diem receipts. The failure resulted in nonrecognition in this case of what the Commission in the opinion from which we have quoted stated as a fact, that "if per diem is more . . . than car ownership costs, a substantial difference can result:

a difference which represents actual dollars . . . received.'"

The indefensibility of the appellees' position can be demonstrated by supposing that railroad interchanges operated a little differently from the way they do. If L. & N. crews were used to operate the coal trains in this movement over some or all of the Southern's tracks, and the Southern paid the L. & N. somewhat more for their services than the L. & N. paid to the crews in wages, we doubt that the appellees here would be arguing that the excess of the payment was not an effective offset to the L. & N.'s costs of rendering the service involved. To make the point a different way, if there were no per diem payments at all, there can be no doubt that the L. & N. would claim, and the Commission in prescribing divisions would allow, its full car costs, on-line and off-line, for a movement in which only its cars were used.

The situation here is no different in principle. The L. & N. is entitled to recoup its full car costs from the coal traffic revenues. An offset to those costs, however, is provided by the L. & N.'s rental payments. In this case the Commission has allowed that offset but only to the extent that the rental payments equalled the costs incurred by the L. & N. when the cars were off its line. It has not explained, and the appellees have not adequately explained—even were they entitled to do so independently of the Commission—why the full offset should not be given effect.

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[7] See also Motor Vehicles—Wayne & Wixon, Mich., to Milwaukee, Wis., 323 I.C.C. 266, 272 (1964).

CONCLUSION

The motions to dismiss should be denied and probable jurisdiction of the appeal noted.

Respectfully submitted,

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